

Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 ISO-00 AID-05 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 USIA-06 XMB-02 OPIC-03 SP-02

CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

CEA-01 PA-01 PRS-01 /089 W

----- 056323

R 221720Z OCT 76

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 6877

TREASURY DEPT WASHDC

INFO AMEMBASSY BONN

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

USMISSION OECD PARIS

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DEPARTMENT PASS FEDERAL RESERVE BOARD

E.O. 11652: N/A

TAGS: EFIN, UK

SUBJECT: GOVERNOR OF THE BANK OF ENGLAND'S MANSION HOUSE
ADDRESS

SUMMARY: THE GOVERNOR OF THE BANK OF ENGLAND, GORDON RICHARDSON, SAID THAT BRITAIN MUST LIVE WITHIN HER MEANS AND AVOID FURTHER BORROWING BOTH FOREIGN AND DOMESTIC. HE URGED THAT THE MONEY SUPPLY (M3) TARGET BE SET BELOW 12 PERCENT IN THE COMING FISCAL YEAR. AN END TO THE EROSION OF STERLING, BOTH INTERNAL AND ON THE FOREIGN EXCHANGE MARKETS WAS BRITAIN'S "GREATEST REQUIREMENT" ACCORDING TO THE GOVERNOR. MANY OBSERVERS CONSIDER THE SPEECH TO BE THE FINEST RICHARDSON HAS EVER MADE. END

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SUMMARY

1. FOLLOWING UP THE CHANCELLOR'S SPEECH TO THE SAME MANSION HOUSE AUDIENCE (SEE SEPTTEL) BANK OF ENGLAND GOVERNOR GORDON RICHARDSON STRONGLY DEFENDED THE FINANCIAL COMMUNITY AGAINST THE CHARGE THAT IT HAD FAILED BRITISH INDUSTRY AND SHOULD THEREFORE COME UNDER SOME FORM OF STATE OWNERSHIP. HE CITED THE 1.0 BILLION POUNDS OF EXPORT EARNINGS ON INVISIBLES EARNED BY THE CITY OF LONDON PLUS THE 1.75 BILLION POUNDS OF NEW EQUITY ISSUES FLOATED SINCE THE BEGINNING OF 1975 AS EVIDENCE OF THE CITY'S IMPORTANT CONTRIBUTION.

2. WITH REGARD TO THE CURRENT ECONOMIC SITUATION, THE GOVERNOR PRAISED THE CHANCELLOR'S DECISION TO GIVE PRIORITY TO REDUCING INFLATION, TO SHIFT RESOURCES INTO THE BALANCE OF PAYMENTS AND INVESTMENT, AND TO RESTRAIN CONSUMPTION. HOWEVER, HE SAID THAT PROGRESS HAD NOT BEEN RAPID ENOUGH.

3. MR. RICHARDSON SPOKE OF THE APPLICATION FOR FURTHER BORROWING FROM THE IMF, BUT SAID IT WAS NOT A SOLUTION TO THE PROBLEM. RATHER THE SOLUTION DEPENDED UPON BRITAIN AGAIN LIVING WITHIN HER MEANS, THUS CEASING TO HAVE TO GO INTO DEBT TO FOREIGN LENDERS.

4. THE GOVERNOR SUGGESTED THAT THE SETTING OF MONETARY TARGETS IN CONJUNCTION WITH FISCAL POLICY WAS CORRECT. HE CALLED FOR AN M3 TARGET BELOW 12 PERCENT IN THE COMING FISCAL YEAR AND SAID THAT CURRENT STANCE OF MONETARY POLICY WILL HAVE TO CONTINUE FOR THE TIME BEING. IF HIGH INTEREST RATES WERE TO CONTINUE FOR LONG, INVESTMENT WOULD SLOW AND HMG WOULD HAVE TO CHOOSE BETWEEN REDUCING PUBLIC SECTOR BORROWING OR SEEING A RECOVERY IN INVESTMENT ABORT. WITH REGARD TO THE BALANCE OF PAYMENTS, HE SAID THAT EARLY EVIDENCE OF AN IMPROVEMENT WAS NECESSARY AND THAT "IF IT REQUIRES A FURTHER DEGREE OF AUSTERITY TO GUARANTEE THIS, I BELIEVE WE SHALL HAVE NO OTHER CHOICE THAN TO ACCEPT IT.

5. KEY EXCERPTS FROM THE GOVERNOR'S SPEECH INCLUDE:
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QUOTE MONETARY AND FISCAL POLICY -- AND I WOULD ADD INCOMES POLICY -- EACH HAVE THEIR PART TO PLAY, AND SHOULD FORM A COHERENT WHOLE. AT PRESENT THERE IS, UNDENIABLY, A GROWING QUESTION OVER THE BALANCE BETWEEN OUR MONETARY AND FISCAL STANCES. THE RECORD LEVEL OF INTEREST RATES REFLECTS IN LARGE PART THE DIFFICULTY OF FINANCING, WITHOUT EXCESSIVE MONETARY EXPANSION, THE PRESENT PUBLIC BORROWING REQUIREMENT. THE CURRENT STANCE OF MONETARY POLI-

CY WILL HAVE TO CONTINUE FOR THE TIME BEING. BUT IT
IS FAR FROM COSTLESS AND IF INTEREST RATES REMAIN SO HIGH
FOR LONG THEY WILL BEGIN TO BE A POWERFUL DETERRENT TO
INVESTMENT, ONLY NOW SHOWING SIGNS OF RECOVERY. IN THAT
CASE, AS THE CHANCELLOR HAS POINTED OUT, ONE WOULD HAVE
TO ASK WHETHER THIS IMPACT ON INDUSTRIAL REVIVAL WAS
ACCEPTABLE OR WHETHER PUBLIC SECTOR BORROWING SHOULD NOT
BE REDUCED MORE RAPIDLY, SO AS TO PROVIDE MORE SCOPE FOR
THE BORROWING OF INDUSTRY.

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CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05 SS-15 STR-04

CEA-01 PA-01 PRS-01 /089 W

----- 049993

R 221720Z OCT 76

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 6878

TREASURY DEPT WASHDC

INFO AMEMBASSY BONN

AMEMBASSY PARIS

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QUOTE THE BALANCE OF PAYMENTS DEFICIT TO WHICH I HAVE AL-
READY ALLUDED IS AN ADDITIONAL REASON FOR ASKING WHETHER

A QUICKER REDUCTION OF PUBLIC BORROWING WILL NOT BE NEEDED. THE BALANCE OF PAYMENTS IS NO DOUBT SET TO IMPROVE, MORE ESPECIALLY OVER A SPAN OF YEARS. BUT WE NEED EARLY EVIDENCE OF SUCH IMPROVEMENT. IF IT REQUIRES A FURTHER DEGREE OF AUSTERITY TO GUARANTEE THIS, I BELIEVE WE SHALL HAVE NO CHOICE BUT TO ACCEPT IT.

QUOTE OUR GREATEST REQUIREMENT IS THAT WE SHOULD PUT A STOP TO THE DEBILITATING EROSION IN THE VALUE OF OUR CURRENCY, EXTERNAL AND INTERNAL. IT IS CLEAR ENOUGH HOW INFLATION SAPS CONFIDENCE, INCREASES UNCERTAINTY AND DELIMITED OFFICIAL USE

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STROYS INITIATIVE. IT ALSO DESTROYS EMPLOYMENT. IT WOULD BE EASIER TO EXPAND EMPLOYMENT IF IT WERE PLAIN THAT THE PACE OF COST AND PRICE INCREASES WAS BEING REDUCED. IS THERE NOT HERE OPPORTUNITY FOR CONTINUED COLLABORATIVE EFFORT TO BRING TOGETHER THESE IMPERATIVES -- LESS INFLATION, BUT MORE EMPLOYMENT? IT CANNOT BE TOO WIDELY UNDERSTOOD THAT WHAT PACE OF EXPANSION WE CAN AFFORD, WILL TURN ON HOW QUICKLY INFLATION CAN BE OVERCOME. UNQUOTE

6. COMMENT: BEGIN LIMITED OFFICIAL USE MANY OBSERVERS PRESENT CONSIDERED THE RICHARDSON SPEECH THE BEST HE HAS EVER MADE. HE DID NOT HEDGE, CLEARLY STATED HIS VIEWS, AND CLEARLY REFLECTED THE MOOD OF HIS AUDIENCE, WHEN IN CONCLUSION, HE REMARKED, "UNLESS I ERR GREATLY, PEOPLE EVERYWHERE LONG FOR AN END TO THE HUMILIATION OF OUR DECLINE AND ARE READY FOR THE STRUGGLE." RICHARDSON ALSO BUILT SPECIFICALLY ON THE CHANCELLOR'S COMMENT ABOUT THE POSSIBLE NEED FOR MORE RAPIDLY REDUCING PUBLIC SECTOR BORROWING. READING BETWEEN THE LINES, THE GOVERNOR CLEARLY INDICATED THAT MONETARY POLICY IS CARRYING TOO HEAVY A SHARE OF THE BURDEN AND THAT SACRIFICES IN OTHER AREAS ARE CALLED FOR.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, SPEECHES, BANKS
Control Number: n/a
Copy: SINGLE
Draft Date: 22 OCT 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: ElyME
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976LONDON17035
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D760397-0607
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t19761024/aaaaaund.tel
Line Count: 211
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: ElyME
Review Comment: n/a
Review Content Flags:
Review Date: 07 APR 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <07 APR 2004 by ElyME>; APPROVED <04 AUG 2004 by ElyME>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: GOVERNOR OF THE BANK OF ENGLAND'S MANSION HOUSE ADDRESS SUMMARY: THE GOVERNOR OF THE BANK OF ENGLAND, GOR
TAGS: EFIN, UK, (RICHARDSON, GORDON)
To: STATE TRSY
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006